

# COST *and* MANAGEMENT

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THE CANADIAN SOCIETY OF

COST ACCOUNTANTS & INDUSTRIAL ENGINEERS

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L. J. Brooks, R.I.A., Interim Secretary-Manager and Editor

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at 25 cents each.

# EDITORIAL

During the past five months, I have had the honor and pleasure of serving the Society in the capacity of Interim Secretary-Manager and in doing so have gained many friends and an insight into the complex set-up of our Society.

It is with regret that I was unable to accept the proffered appointment as permanent Secretary-Manager, since I am a practising public accountant with a fairly extensive practice.

In the last few issues of "Cost & Management" I have tried to introduce articles which I believed to be of interest to the members, and in this issue an article on taxation appears which covers the recent amendments and gives several comparative tables. Mr. H. P. Wright, R.I.A., who has kindly given his consent to the printing of this article is to be complimented on its completeness and excellence.

It is with great regret that I have to announce that this will be the last issue of the magazine which I will edit in my present capacity, and I take this opportunity to thank all the members who have contributed and forwarded articles to me.

It is my pleasure to extend to all Provincial Societies and Chapters my best wishes for their continued success, with the hope that they will attain the full recognition that they have worked for and so richly deserve.

As your Interim Secretary-Manager, I have conscientiously tried to fulfill the obligations of that important office and regret that there are many matters which I shall not be able to follow through to completion. However, I carried on at a very difficult time and if my services have contributed something to the Society and its members, I shall feel justly proud.

It is my earnest wish that you will extend to your new Secretary-Manager the same co-operation and good will that you have so willingly given to me.

On behalf of the President, the Directors of the Society, and myself, I wish to extend to all the Compliments of the Season.

L.J.B.

## COST AND MANAGEMENT

### New Members

#### Montreal.

- K. E. Morrison, Noorduyn Aviation Limited.
- A. W. Hamilton, Haskell, Elderkin & Co., C.A.
- Stanley Wickes, Northern Electric Co. Ltd.
- J. E. Paisley, Gazette Printing Co. Ltd.
- J. A. McLaren, Defence Industries Ltd., Villeray Works.
- C. H. Dyke, Fairchild Aircraft Ltd.

#### Quebec.

- L. E. Boutin, Dept. of Finance, Comptroller of the Treasury.
- R. S. Langlois, International Business Machines.

#### Windsor.

- Graham C. Ferguson, Burroughs Adding Machine of Canada Ltd.
- Joseph M. Smith, B.A., Gelatin Products Limited.

#### Kitchener.

- Thomas Padden, Dominion Rubber Co. Ltd., Naugatuck Chemicals Division, Elmira.
- H. B. Miller, Dominion Rubber Co. Ltd., Naugatuck Chemicals Division, Elmira.
- John A. Merklinger, The L. McBrine Co. Ltd.
- Carl Israel, The L. McBrine Co. Limited.

#### Toronto.

- John Petersen, Nerlich & Company.

#### Niagara

- E. S. Jones, Plymouth Cordage Ltd.

#### Edmonton.

- R. Forrest, Edmonton Cold Storage Co. Ltd.

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### Personal

Congratulations are in order for Mr. Samuel E. Diamond, F.C.I., on his election as President of the Canadian Exporters' Association.

The Secretary's office has been notified of the following appointments to the Dominion Educational Co-ordinating Committee:

The Society of Industrial Accountants of Alberta—Mr. F. G. Winspear, C.A., R.I.A.

The Society of Industrial Accountants of B.C.—Mr. N. J. C. MacKinnon.

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### Back Numbers Wanted

The following back numbers of Cost and Management are urgently required:

April, 1936.

August, 1936.

May, 1936.

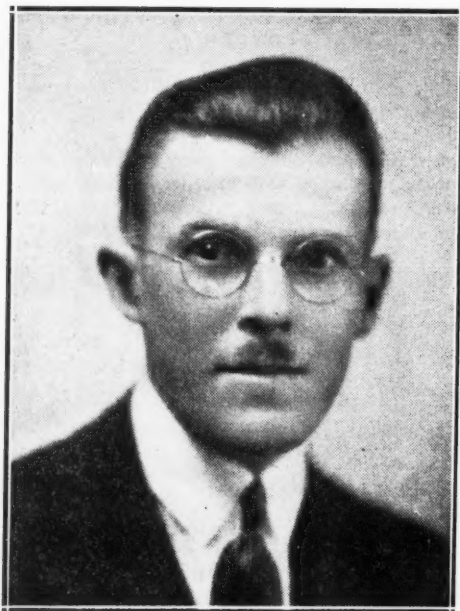
December, 1936.

July, 1936.

January, 1937.

Any member who can spare any of the issues listed is urged to mail same immediately to the Secretary.

COST AND MANAGEMENT



D. R. PATTON, C.A., L.C.M.I.

Haskell, Elderkin & Co., C.A.

Montreal, Quebec.

Chairman

Dominion Educational Co-Ordinating Committee.

## COST AND MANAGEMENT

### Chapter Notes

#### Vancouver.

The November meeting of the Chapter was held at the Hotel Georgia on November 9th, 1944.

The speaker was Mr. V. E. Feimann, C.G.A. comptroller of the British Columbia & Dredging Co. Ltd. and his subject was "Cost Problems and Cost Control in Construction."

#### Fort William-Port Arthur.

The regular monthly meeting of the Chapter was held in the Royal Edward Hotel on Thursday, November 23, 1944.

The speaker was T. W. Tod, Manager, Bank of Montreal, and his subject was "Recent Changes in the Bank Act."

#### Hamilton.

The November meeting of Hamilton Chapter was held in the Royal Connaught Hotel on Thursday, November 30, 1944.

The speaker was Mr. T. M. Moran, C.E., Toronto, Manager Stevenson & Kellogg, Ltd., and his subject was "Some Aspects of Industrial Engineering as Related to Organization."

#### Toronto.

The regular monthly meeting of the Chapter was held at Malloney's Art Gallery, on Wednesday, November 15th, 1944.

The speaker was Mr. William F. Jackman, Accounting Supervisor, The Eastman Kodak Co. Ltd., Rochester, N.Y., and his subject was "Cost Accounting and Control in To-morrow's Competitive Economy."

The meeting took the form of a joint meeting with the Hamilton Chapter.

#### Windsor.

The November meeting of the Chapter was held at the Norton-Palmer Hotel on November 23, 1944.

The speaker was Mr. H. J. Dustan, B.A., Manager of the Windsor Branch, Bank of Nova Scotia. His subject was "Section 88 of the Bank Act, and the Bills of Exchange Act."

#### Kitchener.

The regular monthly meeting of the Chapter was held at the "Coffee Bar", Preston, Ontario, on November 30th, 1944.

The speakers were Mr. P. H. Hohman, Mr. G. L. Hunt, and Mr. D. G. Seebach, R.I.A., and the subject was "An informal discussion of Bedeaux, from the establishing of rate to pay cheque and General Ledger."

#### London.

The November meeting of the Chapter was held at the Hotel London on Thursday, November 30th, 1944.

The speaker was Mr. W. R. Yendall and his subject was "Reduction of Tax Load on Canadian Business."

COST AND MANAGEMENT



HAROLD P. WRIGHT, R.I.A.

Wright, Pounder & Co.

Hamilton, Ontario.

Chairman of the Educational Committee

The Society of Industrial & Cost Accountants of Ontario.

## 1944 TAX AMENDMENTS

### Montreal.

The regular monthly meetings of the Chapter were held on November 10, 1944, and November 24, 1944, at the Mount Stephen Club.

The speakers and their subjects were:

November 10, 1944—R. F. Thompson, Director of Training, Dept. of Labour, "Training of Employees."

November 24, 1944—W. S. Lecky, Renegotiation Officer, Dept. of Munitions & Supply, "Fair and Reasonable Profits in War Business."

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## 1944 Tax Amendments

By HAROLD P. WRIGHT, F.A.C.S. (Eng.), R.I.A. (Ont.)

Senior Partner

WRIGHT, POUNDER & COMPANY

Corporate Accountants

Many of our members have frequently suggested that our monthly publication should contain a resume of amendments to the Income & Excess Profits Tax Acts from time to time and, with that thought in mind, I have prepared this article as an experiment. It is to be hoped that our Magazine Committee will receive suggestions and criticisms as a result thereof, so that future policy along these lines may be intelligently considered by that body.

I believe it important to call to the reader's attention that no reference has been made to the many sections of both acts which have not been the subject of amendments this year, nor to the vexatious question of interpretation and departmental rulings issued to assessors, which do not get into the hands of practising accountants or the public.

I am aware that tax returns for certain corporations are, in many cases, made out by our members for their own particular firm, and the information contained herein should not in any sense be considered a guide for the preparation of tax returns generally.

In the preparation of explanatory notes, I have had occasion to make numerous references to "The Dominion of Canada Taxation Service" published by Richard De Boo Limited of Toronto, and I am indebted to them in no small measure for the clear and concise way in which they deal with this particular phase of taxation.

The 1944 Budget was brought down in the House of Commons on June 26th last, and, except for minor changes, received Royal Assent on August 15th. There appears to be little immediate relief from the present enormous tax burden, and certain proposals, with a view to providing increased employment in the post-war period, are indefinite as to the date of application, with the obvious result that business firms have nothing concrete upon which to justify the risking of additional capital.

Highlights of the Budget affecting Income Tax of individuals are summarized hereunder:

## COST AND MANAGEMENT

- (a) Compulsory savings portion of the tax is suspended, commencing July 1, 1944.
- (b) Alimony payments may be deducted from income, in lieu of the tax credit previously allowed.
- (c) Tax allowance for dependents is extended to include "in-laws" and children actually dependent on the taxpayer for support, including illegitimate children.
- (d) Allowance for medical expenses has been extended to include expenses incurred outside of Canada, and a taxpayer may claim for any twelve months' period ending in the calendar year.
- (e) Lump sum payments to employees upon retirement may be spread by them over five years for income tax purposes.
- (f) Companies authorized to accept deposits will be required to file returns showing interest credited to depositors' accounts.
- (g) Refundable portion of "Compulsory Savings" withheld by the Crown is to be repaid to persons over 65, provided the annual income of such persons is less than \$5,000.00.
- (h) Interest on unpaid taxes, before assessment, is reduced from 5% to 4%.
- (i) Assessments are not to be re-opened after six years from the date thereof, except in cases of fraud or misrepresentation.
- (j) Provision is made for the appointment of a Royal Commission to advise on the taxation of life annuities and to consider the question of hardship arising out of income tax and succession duties payable on the death of the chief shareholder of a "private company", which has a large amount of undistributed earned surplus.
- (k) Individuals may reduce their income for taxation purposes by gifts in money to the Crown, with the proviso that such gifts are in lieu of allowances for charitable donations.

Highlights of the Budget affecting Incorporated Companies, Partnerships and Proprietorships follow:—

- (1) Losses may be carried back one year and carried forward three years.
- (2) Standard profits of Corporation to be adjusted upward to the extent of 5% of any increase in capital employed since the commencement of the Excess Profits Tax Act.
- (3) New businesses will not be subject to the 100% rate under the Excess Profits Tax Act for the first year of operation.
- (4) Double depreciation is to be allowed on new capital investments to encourage reconstruction projects, until December 31, 1946, or until two years after the cessation of hostilities with Germany, whichever is the earlier.
- (5) Expenditures for scientific research are to be allowed as a deductible expense.
- (6) Expenditures on repairs and maintenance to the extent of one-half thereof may be charged against the profits of previous fiscal years ending after December 31, 1942. The period when such expenditures will qualify is to be fixed by the Government in Council.
- (7) Refundable portion of Excess Profits Tax may be assigned as se-



## 1944 TAX AMENDMENTS

curity for a loan, where funds are required for conversion to peace time production and where they will provide substantial employment.

- (8) Dividends received from a wholly owned non-resident subsidiary are to be exempted from tax when received by the Canadian parent company.
- (9) Provision is made for tax credits of 50% of expenditure under certain conditions on deep test oil wells which prove to be non-productive.

### COMPARATIVE TAX TABLE

The amount of tax contribution to the Crown is fairly well known by each individual in his own income bracket, but the substantial increase in rates on rising incomes has not been given much publicity. The following table indicates the tax payable by married persons with no dependents, in certain income groups, as applied to Canada, the United States, and Great Britain, and, while the compulsory savings portion of the Canadian Tax was not discontinued until July 1, 1944, this table eliminates the savings element in all cases and wherever applicable, so that each country is on a comparable basis:

Income	Canada	United States	Great Britain (\$4.45 to the £)
\$ 600 .....		\$ 2.00	
750 .....		6.00	
1,000 .....		12.00	\$ 25.00
1,250 .....\$	18.00	46.00	93.00
1,300 .....	31.00	57.00	106.00
1,400 .....	65.00	77.00	133.00
1,500 .....	101.00	98.00	160.00
1,800 .....	170.00	160.00	244.00
2,000 .....	229.00	202.00	327.00
2,500 .....	399.00	305.00	535.00
3,000 .....	582.00	411.00	743.00
4,000 .....	964.00	635.00	1,161.00
5,000 .....	1,378.00	975.00	1,577.00
7,500 .....	2,520.00	1,720.00	2,687.00
10,000 .....	3,762.00	2,585.00	4,047.00
15,000 .....	6,929.00	4,695.00	7,178.00
20,000 .....	10,279.00	7,315.00	10,601.00
30,000 .....	17,446.00	13,485.00	18,141.00
50,000 .....	32,813.00	27,585.00	35,135.00
75,000 .....	53,497.00	47,595.00	58,257.00
100,000 .....	75,247.00	69,435.00	82,282.00
150,000 .....	121,214.00	115,415.00	131,082.00
200,000 .....	167,214.00	161,905.00	179,982.00
500,000 .....	443,214.00	443,895.00	472,282.00
1,000,000 .....	903,214.00	900,000.00	(Not Calculated)

The above is based on "earned income" and additional taxes are payable on investment income over the basic exemption of \$1,500.00.

At first glance it may appear that residents of the United States get off

## COST AND MANAGEMENT

somewhat more easily than ourselves, but it must be remembered that State taxes are assessable against income in all States other than Connecticut, Florida, Illinois, Maine, Michigan, Nebraska, Nevada, New Jersey, Ohio, Pennsylvania, Rhode Island, Texas, Washington and Wyoming. If, for instance, you live in New York, you are liable to a State tax of from 2% on the first \$1,000 of taxable income to 7% on and over \$9,000 after deducting a basic exemption of \$2,500.00.

## SUCCESSION DUTIES

Only minor changes have been made in the Federal Act in the present Budget resolutions.

The impact of Provincial and Federal Succession Duty taxes is not generally known, and The Manufacturers Life Insurance Company have kindly given their consent to the reproduction of a table giving the approximate Succession Duty Taxes payable to the Governments of Ontario and the Dominion respectively, where an estate passes to the deceased's wife in its entirety and there are no dependents.

Net Taxable Estate	Province of Ontario	Dominion Government	Total Taxes
\$ 25,001 .....	\$ 287.50	\$ 150.03	\$ 437.53
35,000 .....	644.00	570.00	1,214.00
50,001 .....	2,300.00	1,500.05	3,800.05
60,000 .....	3,174.00	2,120.00	5,294.00
75,001 .....	4,743.82	3,300.06	8,043.88
85,000 .....	6,158.25	4,192.50	10,350.75
100,001 .....	8,625.00	6,000.07	14,625.07
115,000 .....	10,315.50	7,837.50	18,153.00
125,000 .....	11,500.00	9,292.50	20,792.50
135,000 .....	12,730.50	10,867.50	23,598.00
150,001 .....	14,662.60	13,650.10	28,312.70
300,001 .....	34,500.00	37,800.13	72,300.13
500,001 .....	71,875.00	79,200.16	151,075.16

The above table does not constitute a basis on which the taxation applicable to an individual estate can be determined; it is, however, indicative of the extent to which the combined Dominion and Provincial Succession Duty taxes can deplete the principal of an estate.

## AMENDMENTS TO THE INCOME WAR TAX ACT

Submitted hereunder in chronological order is a summary of additions and amendments to the various sections of the Income War Tax Act which implement the Budget resolutions:

### Section "2"

Expenditures under the heading of scientific research are defined, together with the clarification of the meaning of "taxation year" and "taxation period."

Dependents are extended to include parents-in-law, grandparents-in-law, brothers-in-law, sisters-in-law, sons-in-law and daughters-in-law in the same circumstances and subject to the same conditions as parents, grandparents, brothers, sisters, sons and daughters respectively. The provision under which a tax credit is allowed in respect of a child of the taxpayer is extended to include an allowance in respect of any person under 18 years of

## 1944 TAX AMENDMENTS

age and dependent upon the taxpayer for support, including an illegitimate child.

### Section "3"

Payment by an employer to an employee upon retirement, other than a payment out of a superannuation or pension fund or plan, if the Minister of National Revenue is satisfied that such payment is in recognition of long service, may be deemed to be income of the retired employee over a period of five years rather than income in the year when received.

Income may be reduced by the amount of a gift to His Majesty. In the case of a taxpayer whose wife is in receipt of unearned income in excess of \$660.00 it would now appear that she may pay such excess over to His Majesty in the right of Canada. This course would apparently put the husband in the position of being able to claim the \$150.00 tax credit under the graduated rate together with a saving of one or two percent on his total income for purposes of normal tax. Such a gift on the part of a wife would be beneficial only to the extent of the maximum savings effected by reduction in the husband's tax liability.

### Section "4"

Provision is made to give women members of the Armed Forces the same tax exemption as the men.

The income of certain housing projects under the National Housing Act is to be exempted from tax.

### Section "5"

In addition to the \$300.00 allowed as a deduction in each year in connection with an employee's superannuation or pension fund or plan, provision is made permitting payments of a like amount on account of arrears. A member of a Trade Union is now permitted to deduct an amount up to but not in excess of \$300.00 in the form of union dues paid by him to a superannuation or pension fund or plan approved by the Minister.

Charitable donations made on and after February 1, 1944, by a corporation in excess of the average for the last two fiscal periods ending before July 1, 1942, will be allowed at the 40% rate of taxation only. In a statement made in the House of Commons by the Minister of Finance on February 18th, last, he indicated that the modification was intended to enable business concerns to continue, without loss of tax advantage, the level of charitable givings which they had established prior to the coming into force of the 100% Excess Profits Tax rate.

The provision whereby a special payment by an employer to make up a deficiency in an employee's superannuation or pension fund or plan may be deducted from income over a ten-year period has been amended to permit annual payment of one-tenth, or less, of such deficiency to be deducted from income in the year of payment.

The allowance in respect of unusual medical expenses is extended to include expenses incurred outside of Canada.

The deduction allowed in respect of unusual medical expenses is extended to allow as a deduction in any taxation year expenses actually paid in any twelve months' period ending in the taxation year.

Medical expenses are allowed in excess of 4% (instead of the previous 5%) of the income of the taxpayer, not exceeding the aggregate of \$600.00 in the case of a single person, or \$900.00 in the case of a married person

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or persons given an equivalent status, and \$150.00 for each dependent but not exceeding \$600.00 in respect of such dependents. This increases the maximum deduction heretofore allowed by one-half and permits deduction of such expenses in excess of four percentum instead of five percentum of income.

Losses sustained in 1944 and fiscal periods ending therein and all subsequent periods by any person carrying on business may be deducted from profit derived from the business either in the year immediately preceding or in the three years immediately succeeding the taxation year. "Person" under the definitions in Section "2" is deemed to include a corporation, association or other body, etc.

Amount paid pursuant to a decree, order or judgment made in an action or proceeding for divorce or judicial separation, or pursuant to a separation agreement, as alimony or other allowance for the maintenance of the recipient thereof or of the children of the marriage, may be deducted from the income of the payer in lieu of the tax credit previously allowed.

Expenditures for scientific research directly or indirectly related to the taxpayer's business, whether of a current or capital nature, are allowed as a deductible expense in the year when the expenditures are made, except in the case of expenditures of a capital nature, which may be written off over a three-year period commencing with the year of expenditure. It would appear from the reading of paragraph (u) of Section "5" that the Minister has considerable jurisdictional power and it would seem advisable to obtain the consent of the taxing authorities before proceeding on any outlay of this nature where a doubt might arise as to its propriety under this sub-section.

One-half of expenditures on maintenance and repairs incurred by any taxpayer carrying on business, (or on underground developments, in the case of a taxpayer operating a mine), in a period to be fixed by Order in Council, may be regarded as deferred maintenance and repairs and deductible as an expense, at the option of the taxpayer, either in the year or fiscal period when incurred or in years or fiscal periods ending after December 31, 1942. The Government apparently recognizes that in many instances plant and machinery have not been maintained up to a reasonable standard, chiefly on account of a shortage of skilled labour and replacement parts. Reserves set up for this specific purpose have never been allowed by the taxing authorities by reason of Section "6" (1) (d).

A taxpayer who is totally blind or a taxpayer who is totally blind at any time during the taxation year, has the option of deducting \$480.00 of the amount of salary or wages paid to a full time attendant from his income in lieu of the deduction in respect of unusual medical expenses.

### Section "6"

The Minister may allow depreciation at double the rate normally allowed, in respect of bona fide new capital expenditures made after November 10, 1944, provided that the taxpayer will be required to charge in any subsequent year at least one-half the rate normally allowed, and the taxpayer is prevented from realizing any profit on disposal of the said assets by reason of the charging of double depreciation.

### Section "8"

Taxpayers are now permitted to deduct from tax the amount paid to

## 1944 TAX AMENDMENTS

any foreign country for Income Tax in respect of the income of the taxpayer from sources therein, and the previous provision requiring a reciprocal arrangement with such countries is now deleted.

Dividends paid by a wholly-owned subsidiary non-resident Company to a Canadian parent Company are exempt from tax when received by such parent Companies.

The tax credit in respect of contributions for prospecting is continued in force for another year.

With the approval of the Governor General in Council and upon recommendation of the Minister of Mines and Resources, expenditures incurred by a corporation, association or syndicate or exploration partnership whose business is production, refining or marketing of petroleum or exploration or drilling for petroleum, provided the well is spudded between June 26, 1944, and March 31, 1945, and further provided that the well is a deep test well the drilling of which is desirable for Canada, and is one which would not have been undertaken but for this tax credit, such expenditures, to the extent of 50% thereof, may be deducted from the tax otherwise payable.

### Section "33"

Income of a deceased person up to the date of his death must be contained in an Income Tax return to be filed within six months of the decedent's death. This will enable his estate to be cleared by the Income Tax authorities at an earlier date than has heretofore been possible, since the return in many cases did not have to be filed until April 30 in the year following death, which, in some cases, might be one day short of sixteen months after the actual date of death.

### Section "39"

Persons authorized by law to accept deposits are required to file information returns showing interest credited to depositors in 1944 and subsequent years. These returns are to be filed on or before the last day of February in each year without any notice or demand being made.

### Section "46" A

This is a new section and deals with the keeping of records by persons required to pay or collect taxes.

1. Every person carrying on business who is required to pay or collect taxes must keep records and books of account at his place of business in Canada or at such other place as the Minister may designate, in such form and containing such information as will enable the amount of taxes or other sums that should have been paid or collected to be determined.

2. Requires that these records be kept until the written permission of the Minister has been obtained for the disposal of the said records.

3. Requires that the records be available for inspection at all reasonable times to officers of the Department of National Revenue and other authorized persons.

4. Authorizes the seizure of the said records for violation of the Act.

5. Provides a penalty of not more than \$1,000.00 and not less than \$5.00, and in default of payment a term of imprisonment of not more than 12 months, to every person who fails to keep records and books of account as required under this section of the Act, and Sub Section 6 imposes a penalty of not less than \$200.00 and not more than \$2,000.00, or imprison-

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ment of not more than 6 months, or both penalty and imprisonment, for failure to make records and books available to authorized persons.

### Section "48"

Interest payable on taxes not paid when due is reduced from 5% to 4% per annum.

### Section "55"

This section has been entirely re-written and now limits, to a period of six years from the date of the original assessment, additional assessments by the Minister, except where the taxpayers have made any misrepresentation or committed any fraud in making returns or supplying information under the Act. This brings the Canadian law into line with the practice followed in the United States and Great Britain. Primarily it would seem that the Section now benefits the honest taxpayer, and it does not seem that a dishonest citizen will have any better chance of consolidating any illegal gain than heretofore.

### Section "58"

Members of the armed forces overseas are to be allowed a period of one year after the day when such person ceases to be on the strength of such a unit, or later with the consent of the Minister, for serving a notice of appeal upon the Minister of National Revenue in respect of the taxation year of 1939 and subsequent years.

### Section "77"

With respect to returns filed in 1944 and subsequent years, the penalty for failure to file on time is reduced to 5% of the amount of tax unpaid at the date when the return was due. There is a minimum penalty of \$5.00 and a maximum penalty of \$500.00. This replaces the previous provision of a 5% penalty on the total tax rather than the balance of the tax.

### Section "80"

This section has been completely re-written and provides penalties for false statements in any return, destroying records and making false entries, attempting to avoid compliance with the Act or to avoid payment of tax imposed. Penalties range from \$100.00 and three months imprisonment to a maximum fine of \$1,000.00, three years imprisonment, and double the tax. Complaints may be laid by the Minister in respect of this section under the criminal code within five years from the time when the matter of the information or complaint arose.

### Section "82"

This is an administrative section implementing the provisions of section 46A and section 80. It provides that officers, etc., of a corporation are a party to offences, that information may be for one or more offences, and that the trial may be heard by any police magistrate or justice of the peace if the accused is within their territorial jurisdiction.

### Section "93"

The refundable portion of tax in respect of which a taxpayer is entitled to repayment is to be refunded to a taxpayer when he reaches the age of 65, provided the income of the taxpayer is less than \$5,000.00 in any year thereafter.

### 1st Schedule

The basis of taxation under the normal tax and the tax credit of \$150.00

## 1944 TAX AMENDMENTS

against the graduated tax for a married person is limited to a married person who supports his spouse.

A married person separated from his or her spouse may now claim tax credit for maintaining a self-contained domestic establishment, upon satisfying the same conditions and qualifications now required of an unmarried person in similar circumstances. A taxpayer maintaining one of his children in a self-contained domestic establishment in which he employs a full time housekeeper or servant is now entitled to the tax credit of \$80.00 against the graduated tax and \$28.00 against the normal tax, notwithstanding that he is entitled to the tax credit of \$150.00 against the graduated tax in respect of that child.

Deductions in respect of a dependent child may be made from the tax payable by either of his parents by agreement between them and, if there is no such agreement, the deduction is made from the father's tax unless the Minister otherwise determines; provided that in the case of an illegitimate child the deductions may be made, unless the Minister otherwise determines, from the tax payable by the mother. In the case of a separated person entitled to make a deduction from his income in respect of a payment for the maintenance of a spouse or a child, they shall be deemed not to be the spouse or child of the taxpayer, and the separated person shall therefore be taxed without credit for such dependent.

Provision is made for a deduction of 20% of the amount contributed up to \$400.00 to a daughter or sister under 21 years of age who is a nurse in training.

In applying the tax credit in the case of the armed forces the fixed tax payable remains unchanged as is the case with civilians.

Women members of the forces are granted the same tax credit as the men of the armed forces.

For the taxation year 1944 the total tax of individuals is reduced by one-half the amount of the refundable portion thereof, less one-half credit for savings, and for the taxation year 1945 and subsequent years the total tax of individuals is reduced by the full amount of the refundable portion thereof, less credit for savings.

### AMENDMENTS TO THE EXCESS PROFITS TAX ACT

In several cases the amendments herein are identical with those contained in The Income War Tax Act; they are, however, submitted below in chronological order.

#### Section "3"

Provision is made for relief from the tax at the 100% rate on the profits of the first fiscal period of a new business coming into existence for the first time after June 26, 1944. It would seem that an individual or an Incorporated Company carrying on business could set up a new business and obtain substantial tax advantage, provided it carries on a substantially different business than the one it is already operating and uses therein physical assets substantially different from those used in the present or a previous business carried on by the said individual or Company.

#### Section "4"

An adjustment of the standard profits of corporations is now allowed where there has been an increase in capital employed between 1939 and 1944 through the retention in the business of the profits earned during that

## COST AND MANAGEMENT

period or by other means. The effect of this amendment is to permit an increase in the standard profits of a corporation without the necessity of an equivalent increase in capital stock which was heretofore necessary. In calculating the increase in standard profits, the capital employed at the commencement of the 1939 period is subtracted from the capital employed at the commencement of the 1944 taxation period, and the resulting difference is calculated at 5% and added to the standard profit previously established, after making adjustment for any increase in capital stock for which the standard profit has been increased by 7½% of such capital stock increase. It would further appear that a taxpayer may increase his standard profit by 5% of the increase in capital employed, effected subsequent to any adjustment made by the Board of Referees. In such cases allowance would have to be made for any capitalization of profit for which an allowance has already been claimed at the 7½% rate.

### Section "4A"

This is a new Section and is intended to clarify the law relating to the computation of standard profits with respect to Companies filing consolidated returns under the Income War Tax Act, and it would seem that taxpayers will not be allowed to file consolidated returns for Excess Profits Tax purposes after January 1, 1944, if such election was made subsequent to January 1, 1940.

### Section "5"

Sub-Section "4" of Section "5" has been repealed, and the substitution provides that the Board of Referees ascertain the standard profits of a taxpayer who was not carrying on the same class of business in the standard period as in the year of taxation, in the same manner as if they had not commenced business before January 2, 1939.

### Section "6"

Substitutions and amendments are made, with respect to the profits of taxpayers other than corporations, that the treatment with respect to expenditures for donations, business losses, amount expended on scientific research, deferred maintenance and repairs, depreciation, and amount in lieu of salary are to be calculated in the same manner as provided in the Income War Tax Act for purposes of taxation under the Excess Profits Tax Act.

### Section "9"

Sub-Section "1" has been repealed and the substitution removes the requirement that a foreign country must allow a similar tax credit before a Canadian taxpayer may be allowed a credit for the taxes paid in such foreign country.

### Section "18"

An additional Sub-Section is now added which provides that a taxpayer may assign a refundable portion of Excess Profits Tax where the Governor-in-Council is satisfied that the purpose of the assignment is to enable the taxpayer to make capital expenditures that will contribute to the post-war conversion of the taxpayer's business and that will provide substantial employment. There is a further provision that the refundable portion in the case of bankruptcy, liquidation, winding up or dissolution be repaid in accordance with regulations made by the Governor-in-Council.



## QUEBEC CHAPTER

This latter amendment may not necessarily mean that the repayment will be made at a date earlier than that now prescribed in Section 18.

### First Schedule.

An alteration regarding the deduction of dividends paid during the year from capital employed has been made which provides that the requirement to reduce capital by one-half of the dividends paid in cash during any taxation year be limited only to the extent that earned surplus at the end of the taxation year is less than earned surplus at the beginning of the taxation year.

### Co-Operative Companies.

A test case has been arranged between the Government and the wheat pools, when an interpretation of certain provisions of the Income War Tax Act will be made so as to determine whether the income therefrom is taxable or exempt from tax. It is interesting to note that Great Britain has been taxing co-operatives since 1933 and the question of ability to tax came up by referring the question to a royal commission in 1919, so that it apparently took the British some fourteen years to make up their minds.

No doubt the question of competition with private enterprise will have much to do with the decisions made by law officers of the Government, and there is no doubt that public opinion and pressure from private industry is forcing the whole question to the forefront, but it is not expected that any immediate decision will be forthcoming as it will be well into the year 1945 before the test case between the Government and the wheat pools can be heard.

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## Quebec Chapter Cost and Management Institute

Since July 1st, when members of Quebec had the pleasure of welcoming the members who attended the annual meeting of the Society, they have grouped themselves in a local chapter.

Three meetings have been held since; at one of them the following officers were elected for the 1944-45 term.

President: Andre-J. Dolbec.

Vice-President: Paul-Henri Dorval.

Secy-Treasurer: Charles-H. Robitaille.

Directors: Messrs. L-Paul Duchaine, Geo. Demers, Dominique Bertrand, Maurice Godbout, Romeo Query, Sarto Laliberte and Maurice Rondeau.

On the two other instances, matters of general interest were discussed at round table conferences and proposed by-laws were studied and approved.

It is intended to hold a few meetings during the course of the winter when some members will be called upon to talk on topics of interest relevant to the science of cost and management.

The membership is not yet very large, but present members having already shown a deep interest in the Institute and being most anxious to adhere to all matters dealing with the questions relating to the main objects of the Society, a normal increase is expected.

An agreement entered into with the School of Commerce last spring will be beneficial to both the students and the Society, as it will make it possible for a good many to obtain their L.C.M.I. degree.

## Termination of War Contracts

By W. F. WILLIAMS

Associate Financial Advisor

Department of Munitions and Supply

The Text of An Address Given Before a Meeting of the  
COST AND MANAGEMENT INSTITUTE

For more than five years the Department of Munitions and Supply and its predecessor Boards—The Defence Purchasing Board and the War Supply Board—have been placing contracts with manufacturers for munitions and supplies necessary for waging war. Up to June 30 of this year over 880,000 contracts, having a total value of approximately \$11,500,000,000 had been placed on account of the Governments of Canada, the United Kingdom and other Allied nations. Until now, every emphasis has been on production and, of course, this will continue to be of primary importance until the Pacific war, as well as the European war, has been won.

Within the last year, however, it has been evident that ultimate victory will be ours, although no one can foretell just when V-Day will dawn. As a result, contractors are now becoming more and more concerned with the effect on their business of the wholesale cancellation of these contracts. Heretofore, there has been little need for concern; the Government required all types of equipment, and there was no need to worry about securing orders. All plants were working at capacity, and the problem was not how to get more business but how to get out the orders on hand. Now, however, with mass terminations in sight, every businessman is, or should be, interested in the procedure set up to ensure speedy settlement of claims under such cancellations.

In February of this year, the Department issued for the information and guidance of contractors a Manual of Procedure on Termination of Contracts. This "Blue Book" with which you are, no doubt, familiar was prepared by a Committee consisting not only of officers from the Department but also of representatives from Industry and well-known Chartered Accountants. We felt that the men who have the major part in the preparation of claims to be submitted to the Department following the termination of contracts were particularly well qualified to establish a procedure which would enable settlements fair to the contractor and the Government to be made speedily and yet on a basis consistent with sound business practice.

You are, of course, aware that our Department has been charged with the responsibility not only of procuring the munitions of war and supplies for the Department of National Defence and for Allied Governments, but also for seeing that those supplies and munitions are purchased at fair and reasonable prices. This has involved the setting up of sound procurement policies with which, I am sure, you are all familiar. In many respects, the settlement of a claim, following the termination of a contract, is similar to the negotiations prior to the placing of the contract. There are two essential differences, however. The first is that termination is

## TERMINATION OF WAR CONTRACTS

really procurement in reverse. The second is that even though we may, in spite of all our precautions, pay more for a munition of war than subsequent events appear to justify, the fact remains that we did get something which was urgently required, and thus received value for our money. Upon a termination, however, we will likely receive little, if anything, of value. This will be particularly so in the period of mass termination following the cessation of hostilities.

It is necessary, therefore, that the officer charged with the responsibility of recommending a settlement use even greater care, if possible, than if he were entering into negotiations for the purchase of a shell or gun that was urgently needed.

By Order in Council P.C. 136, dated January 21, 1944, authority has been granted to the Minister of Munitions and Supply to settle claims under terminated contracts by negotiation and agreement with the contractors concerned. By this means, we hope to achieve speedy, final and equitable settlements. This basis of settlement is the normal method adopted by businessmen in their ordinary commercial dealings. It is based on the principle that parties to a contract may negotiate and agree between themselves on the amount to be paid in settlement of their unliquidated obligations. It is important, however, to understand that a negotiated settlement must not be considered as mere horse trading. It must be based upon, and supported by, a record of the facts after a reasonable examination of the claim. This means that a thorough review of the claim presented by the contractor must be made by the settlement officer. It does not necessarily mean that in all cases a complete audit is to be performed. In many cases, an office review of the claim will be sufficient. This probably will be the case where the contractor is known to have installed and maintained adequate accounting and production records.

May I digress for just a moment to stress the importance of maintaining adequate records? The Department of Munitions and Supply Act provides that every person, whether a prime contractor or a sub-contractor, who has entered into a "munition contract," must keep detailed accounts and records of the cost of carrying out such contracts, and that these accounts and records may be inspected and audited at any time by the representatives of the Minister of Munitions and Supply. This establishes the legal responsibility for maintaining such records.

There is, however, another, and, I believe, much more potent argument in favour of maintaining proper records. In the event of termination, the contractor who has put his house in order and knows what his costs are, will be able to prepare his claim in far less time than the contractor whose bookkeeping system consists of a spike on the wall. Moreover, his claim will be much better prepared, clearer, more concise and he will probably have already established, to the satisfaction of the Chief Cost Accountant that his records are such as can be considered reliable, thus enabling the settlement officer to process the claim with a minimum of delay.

It is stated in the Manual that a contractor may be reimbursed for normal spoilage and overages. But what constitutes "normal" spoilage? While in peacetime, spoiled work was frequently tolerated up to 5% or even 10%, under war conditions this loss can, in some abnormal circumstances, rise to even higher ratios. This may be due to untrained labour,

## COST AND MANAGEMENT

lack of familiarity with the operations or machines required for manufacturing a new product, and various other causes. Spoiled work should not be buried in the general overhead expense account. If it is an important element of cost it should be identified contract by contract, if reimbursement is expected. Proper records are essential in order to prove actual spoilage costs under current conditions. Similarly, starting load costs, preproduction charges and other non-recurring expenditures must be substantiated by adequate records. No claim can be processed in a few days or even a few weeks if it is not capable of being readily verified. Speed may be desirable, but it is not the controlling factor. Proper records are important now when comparatively few terminations are occurring. They will be of even greater importance when mass terminations occur, because for many companies the settlements of claims will constitute their sole source of income during the period of transition from wartime to peacetime production. It is essential, therefore, to set up proper records and to organize and train personnel in termination procedure now.

When a Claim or Request for Interim payment is received in the Department it is registered and a settlement officer is assigned to process the claim or recommend an interim payment. This officer, however does not act alone. He is really the captain of a team, consisting of an accountant, a lawyer and production officers, all of whom are consulted from time to time as may be necessary by the settlement officer before he recommends a settlement. He will ordinarily communicate with the contractor at the time he is advised that a Claim will be received following the termination of a contract, and a conference in the early stages of the discussions, even before the preparation of the Claim, is most desirable. In this way, the contractor may, if he is in doubt, be advised as to the manner in which his Claim is to be prepared. He may also receive advice from the settlement officer as to the disposal or retention of many of the items of the inventory. Many contentious problems may be settled across the table in these preliminary discussions.

The representative of the Chief Cost Accountant will have made an examination of the Claim and will have available information as to the adequacy of the records of the contractor. Consequently, he will be in a position to advise the Negotiator as to whether or not a more detailed audit of the claim is desirable, and whether this audit should be conducted by Treasury or by the Company's own auditors under the direction of the Chief Cost Accountant.

In the meantime, the inventory will have been submitted by the settlement officer to production officials of the Department, whose responsibility it is to pass thereon. They are required to certify as to the reasonableness of each item in relation to other items, and to the stage of completion, as well as to the reasonableness of the quantities of materials and work in process on hand in relation to the quantitative requirements of the unfinished portion of the contract. They must also certify that the items are of a type necessary for the execution of the contract, and will arrange for at least a test check of the materials in the inventory. They are also required to pass upon the reasonableness of the charges for jigs, fixtures and such like items, as well as starting load costs, pre-production expenses, spoilage and other items of a similar nature. The commitments to, and

## TERMINATION OF WAR CONTRACTS

settlements with, sub-contractors are, of course, subject to the scrutiny of the settlement officer, but here too he is assisted and guided by production and other advisory officers.

It must be remembered that the settlement officer can only allow in the determination of costs those costs actually incurred, which are clearly identifiable as properly applicable to the uncompleted portion of the terminated contract. Certain costs cannot be admitted. If I name a few of them, it must not be assumed that those to which I refer are the only excluded costs.

Generally speaking, however, these include such things as losses on other contracts, fees and other expenses not directly related to the terminated contract, losses on investments, provisions for contingencies and premiums on life insurance. Other unallowable items are expenses of converting the contractor's facilities to other uses, the loss or expense occasioned by reason of the fact that the contractor negligently or wilfully failed to stop work within a reasonable time after the receipt of the termination notice and costs incurred because of materials or services purchased or contracted for in excess of the reasonable quantitative requirements of the contract.

While it is extremely important to include in claims all items of cost incurred or made with regard to the uncompleted portion of the terminated contract, it is also important, in the interest of speedy settlements, that claims be free from frivolous charges or padding. Attempts to pad claims in order to establish a trading position will result in delays in final settlement and may subject the contractor to charges of fraud.

Prompt payment does not require that the full value of Claims, as submitted by the contractor, must be paid without a reasonable check of the Claim by the settlement officer. Some contractors, when tendering, have submitted bids, which they knew at the time would involve a loss, simply to obtain the contract, to absorb part of their overhead, to keep labour employed, or for other reasons. However, when these contracts are terminated, the Claims submitted have not always been modest. Moreover, examples are not lacking to show that some contractors have not been averse to putting in a larger claim than could be substantiated by the records.

In connection with the submission of costs subsequent to cancellation, the settlement officer will only allow those costs definitely identifiable as pertaining to the terminated contract, or properly attributable to the termination. Many contractors have submitted Claims showing such costs as a percentage of the materials handled or sub-contractors' claims settled. These items ordinarily are part of general overhead and, as such, are usually distributed on the basis of productive labour. Once a contract is terminated, there can be no productive labour, and the distribution of termination costs on a percentage basis will not be allowed. The only exception to this is where the contractor, in accordance with good business practice, and following the suggestion made in the Manual, has established a Department or Division charged with the handling of terminated contracts and claims thereunder, and to which unit all settlement costs are charged. In such case, the costs of this Department or Division may be pro-rated over all terminated contracts on some equitable basis.

Many companies have already gone far in this matter of setting up

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special termination units and in organizing and training personnel to deal with the termination problem. We have been told, however, that many small sub-contractors are, in fact, too small to justify a separate termination unit. They are not too small, however, to devote the same careful consideration to the preparation of termination claims that they gave to the computation of costs in connection with the original tender. This work deserves and should receive the consideration of top executives.

Once he has satisfied himself as to the costs of the various items in the Claim, the settlement officer then comes to what is probably the most difficult thing to determine in the negotiation of a settlement—the amount to be paid to the contractor to compensate him for his work and for the skill and initiative he has employed in connection with the performance of the contract.

In determining the amount of profit to be paid to a contractor following the termination of a contract, the settlement officer has many things to consider. He is limited, however, to allowing profit only to the extent of work actually done by the contractor and materials actually obtained or furnished. He will not allow any profit with regard to work which has not been done, nor will he make any allowance for a profit which the contractor had anticipated had the contract been carried through to completion.

Some contractors appear to feel that this restriction of not allowing compensation in lieu of anticipated profit, had the contract been completed, is unreasonable. I believe a little thought on the subject will convince any reasonable person that such is not the case. A contract placed by our Department for any of the munitions of war is not, I submit, an ordinary business transaction; it is part of the business of waging war, a war for survival in which each must play his part and share the burdens and risks involved. To ask a contractor to be content with compensation for all of the costs he has actually incurred in connection with the contract which has been terminated, and, in addition, a profit on that portion of the contract in respect of which he has actually performed work or rendered services, is not to ask too much.

In arriving at the amount of profit, the settlement officer will judge each claim on its own merits. He is expected to exercise sound judgment and to recommend a profit that is fair and reasonable in the light of all the circumstances.

Among the many things to which he will give consideration are the following:

- The total work required of the contractor and the extent to which it has been completed.

- The relative difficulty of the work which has been done and of that which remains to be done.

- The extent to which engineering work, production scheduling, technical supervision and other special services have been performed by the contractor.

- The extent of the services rendered in procuring raw materials, parts or sub-assemblies. Where this has been merely the purchasing of standard materials and parts, the profit to be allowed should be relatively lower than on that part of the work which required substantial con-

## TERMINATION OF WAR CONTRACTS

tributions in the way of engineering, technical skill, management and supervision.

The extent to which the contractor has arranged a programme of sub-contracting and its importance in the performing of the contract.

The contractor's accounting data as to his costs.

The extent to which the contractor has in accordance with the requisite authority, disposed of materials on hand at the time of termination, thus reducing the amount of his claim.

The extent to which he has verified the claims of sub-contractors and the reasonableness of the settlements that he has arranged with them.

Admittedly, these criteria are in general terms and seem to establish no fixed standards, but in this fact lies the foundation of the negotiated settlement. It preserves a basic flexibility by enabling the settlement officer to engage in a process of "give and take" with the contractor, and leaves him free to arrive at the fairest possible settlement in each situation.

Generally speaking, we try to calculate the profit in dollars and relate it to the work actually performed. It is very difficult, however, to divorce one's thinking from percentages. As a yardstick we feel that the profit should not exceed 5% over all, with not more than 2% profit on raw materials or purchased parts where the contractor has rendered only slight service and no additional work has been performed by him, and a maximum of 7% on work-in-process in his own shop. No profit will be allowed on costs incurred subsequent to the date of termination.

When a Final Claim has been approved, it is necessary to enter into a supplementary agreement between the contractor and the Department before final payment can be made. Once the agreement has been signed, the contractor should submit invoices for the amount agreed upon in the usual manner.

There seems to be some misunderstanding on the part of some contractors as to what the Department expects in their dealings with sub-contractors.

It is extremely necessary, and in many cases urgently so, that the claims of sub-contractors submitted to prime contractors or intermediate sub-contractors above them, receive prompt consideration. Nevertheless, the prime contractor must make a review of each Claim when presented to him. In making this review, he is expected to exercise the standard of scrutiny which he would apply in the conduct of his own affairs. So far as it is possible for him to do so, he should make the same general type of examination of the Claim as is made of his Claim when he submits it to the Government. He is not, however, required to warrant the accuracy of the facts presented to him by the sub-contractor. As a very minimum, he should provide for a review of the Claim by qualified accounting personnel. Based on such office review, it is his responsibility to determine whether any further audit of a particular Claim is necessary. As in all human relationships, the golden rule is the best rule to apply to the sub-contractor's problems.

The importance of this examination and review should not be minimized. While the Government reserves the right to check such statements and demand a refund from the sub-contractor should it be found that the

## COST AND MANAGEMENT

profit allowance is greater than is considered reasonable, as a practical matter we must rely to a great extent upon the contractor's review, because of the sheer volume of work which a review of each settlement with the sub-contractor by the Government would entail. In this, as in other matters, the settlement officer will rely to a great extent upon his past experience with the prime contractor and the knowledge and confidence he has in him.

We expect prime contractors following such review to make immediate settlement with their sub-contractors. In a great many cases, these claims will be small, and I am sure most prime contractors will be glad to get them out of the way. However, where they are substantial, and the prime contractor has not funds immediately available, he should forward them with a Request for Interim Payment to the Department so that, if approved, funds may reach sub-contractors as speedily as possible. You will appreciate that in many cases these sub-contractors are small firms which have not the safe facilities for securing credit that the larger firms have. The procedure in connection with the submission of Requests for Interim Payment provides that any number of Requests may be forwarded, and was designed to take care of situations such as I have outlined.

You are Accountants and Executives, and you will appreciate that upon you will fall the responsibility of preparing Claims, and to a large extent arranging for their settlement. Close co-operation with the settlement officers of the Department, and the training of your own personnel in the preparation of Claims, will do much to expedite their processing and settlement.



## COST AND MANAGEMENT

### Examination Questions

#### INDUSTRIAL ORGANIZATION AND MANAGEMENT

MAY, 1944

Question 1. (10 marks).

In the ordinary corporate structure, what do you understand to be the duties of:

(a) the President, (b) the Secretary, (c) the Works Manager, (d) the Credit Manager, (e) the Personnel Manager.

Question 2. (10 marks).

From time to time, various types of "profit-sharing schemes" are advocated as the solution to certain labour problems. Discuss the merits and demerits of such arrangements from the point of view of the employee.

Question 3. (15 marks).

(a) Outline briefly the basic principles of all wage incentive systems.

(b) An article costs \$3.00, made up as to (a) Material \$1.00, (b) Direct Labour \$1.00 (on a piece work basis), and (c) Overhead \$1.00.

It is proposed to rearrange and speed up the machinery and then to offer the productive workers a bonus of 30c per article if they double their production. What in theory, should be the result, from the standpoint of cost? Why will the theoretical result not necessarily be achieved?

Question 4. (15 marks).

A manufacturing concern uses a staple commodity as its raw material. Its operating statement for the year 1942 is substantially as follows:

Sales .....	1,000,000
Cost of Sales	
Material .....	\$500,000
Direct Labour .....	200,000
Overhead .....	200,000
	<hr/>
	900,000
Manufacturing Profit .....	\$ 100,000

A careful analysis and study of the raw material account shows that 500,000 lbs. were used, at an average cost of \$1.00 per lb., but that there had been a rising market for the material throughout the year and that in fact the market price at the date of sale of the finished product had averaged 25c per lb. above cost.

What conclusions might be drawn from an examination of these facts and figures?

Question 5. (10 marks).

(a) What do you understand by the term "Hedging"?

(b) If a concern sells "Futures" on a commodity exchange, what is its position (i) if prices rise, and (ii) if they decline?

Question 6. (10 marks).

Discuss briefly (a) the advantages and (b) the disadvantages of a system of selling direct from manufacturer to consumer?

Question 7. (30 marks).

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As at 31st December, the current position of a concern which operates a retail store is as follows:

ASSETS	
Cash .....	\$ 50,000
Inventories .....	100,000
	\$150,000
LIABILITIES	
Accounts Payable .....	\$ 40,000
Income Taxes Payable .....	30,000
	\$ 70,000

For the period to 30th June following, its transactions are expected to be substantially as shown hereunder:

	Sales	Purchases	Payments to Suppliers
January .....	15,000	8,000	23,000
February .....	18,000	7,000	18,000
March .....	20,000	12,000	19,000
April .....	25,000	15,000	10,000
May .....	20,000	8,000	12,000
June .....	15,000	9,000	10,000

All sales are on a strictly cash basis and the rate of gross profit averages 30% of the selling price. Expenses paid in cash average \$4,500 per month.

You are required:

- (a) To prepare a monthly cash budget for the period 1st January to 30th June.
- (b) To make an estimate of operating results for the same period.
- (c) To estimate the current position as at 30th June.

## Dehydration Costs

By PHIL GLANZER, A.M.I.E.T., F.A.S.A.

From a wartime standpoint the cost of producing food by dehydration is probably a secondary factor. The essential factor is the production of stable products of high quality that will employ a minimum of shipping space and tonnage. However, if dehydration is to survive as a peace-time method of procession, we are directly concerned with the costs of production, particularly in relation to the production costs of those food preservation methods with which dehydration is likely to compete. These are specifically canning and freezing.

In general, costs may be divided into several categories. Of these categories, the initial or capital outlay includes the cost of a building to house the industry, cost of fruit or vegetable storage, cost of pre-processing equipment and cost of the drying equipment. The capital outlay exclusive of the building for a dehydration unit that will handle approximately thirty tons of potatoes per day should not require an expenditure of over twelve to fifteen thousand dollars.

In comparison with a canning plant of a similar capacity, storage space for the finished goods would be much less. Even if cool storage were required for certain products, such as peas, this cool storage space would be small. In comparison with freezing, the storage costs would be very small.

Pre-processing is, in general similar for the three methods of food conservation and therefore, requires very similar equipment. Certain special methods of pre-processing have been developed for treating leafy vegetables prior to dehydration. These methods have been introduced for the specific purpose of retaining vitamins in these leafy vegetables. Although the addition of such equipment to the pre-processing line adds to the initial outlay, the high vitamin retention in the finished product more than justifies the increased cost.

### Equipment Costs:

The actual drying equipment includes the tunnel, or tunnels, trucks and trays, fans, controls and the heat source. Total equipment for the actual dehydration operation would be more than for canning, but, taking into consideration the requirements of storage, would be less than for freezing.

Dehydration of the prepared product is more expensive than canning as it requires more heat to evaporate water from a product than it does simply to heat a prepared product for sterilization. However, in relation to the cost per dry pound of product, wherein the food value lies whether the food be fresh, dried, canned or frozen, the additional fuel cost for producing the pound of dry product is a very small item. All in all, the capital outlay for a dehydration plant is probably very similar to that required for other processing methods.

### Raw Product Costs:

The second category is the cost of the raw product. If dehydrated goods equal in quality to canned or frozen goods are to be produced, the fresh vegetable or fruit used for dehydration must be at least as good as those

## COST AND MANAGEMENT

used in the canning and freezing trade. With certain products the fresh product should be superior as dehydration necessarily hardens the tissues. A superior product is required if the dehydration of peas, beans and corn is contemplated. These vegetables should be harvested while still very young and tender. It should be emphasized that dehydration cannot make a poor product better and the industry cannot compete with other methods of processing if inferior goods are dehydrated.

The third category of costs lies in the handling of the finished product. It is in this that the chief saving lies. Here there should be a marked saving in packaging, storage and transportation. This can be well illustrated if we consider the costs of production on a product such as apples.

According to the October, 1941, issue of the Economic Analyst, the actual cost of processing apples was 3.15 cents per pound to produce a gallon can (105 ounce tin) of canned apples. This covered the cost of containers, shooks, etc., but the items of overhead, interest, profit, etc., and the cost of the raw fruit were not included.

### Apple Drying Costs:

On the basis of the present increased cost of labour, fuel, etc., these costs would probably be about 5.5 cents per pound dried and around 19 cents per tin canned. A can of apples contains approximately 96 ounces, or six pounds, of actual apple. On this basis the dehydrated product costs less than one cent a pound of prepared apple to produce and canned apples about three cents; or three times as much. When we consider that package costs are approximately one and a half cents per pound for the canned article and not more than a third of a cent for the dehydrated product much of the difference is in package cost. Some of the remainder is covered by the difference between handling apples in segments and in rings.

We may consider the matter of quality. By modern processing methods it is possible to produce a dehydrated article that is very acceptable for pie, apple sauce, or tart manufacture. From January on dehydrated products are as satisfactory as fresh apples for this purpose.

### Compare With the Fresh:

During the past year dehydrated apples have been retailing in Canada at 17 to 20 cents per pound. Approximately five pounds of dried apples are equivalent to the prepared fresh from a bushel of apples. From this figure it is apparent that in the dried form the housewife can buy fruit from 85 cents to a dollar a bushel, a figure much below the market price of fresh or canned apples during any period of the year.

If the dehydration industry is to be of any value to either the fruit grower or processor this must ultimately be corrected. Before the war twenty-five to fifty cents a barrel was paid for processing apples and the dried apples sold as low as seven and one-half cents per pound. Under existing conditions the price has been about thirteen cents to the manufacturer.

If manufacturers in Canada paid a reasonable market price, for example, \$2.50 a barrel for graded fruit, the situation would be something like the following:

### Cost of Producing One Pound of Dried Fruit:

Cost of raw fruit (yield 14 pounds to a barrel) ..... 18c

## DEHYDRATION COSTS

Cost of processing .....	5½c
Cost of packaging in one pound packages .....	1½c
Profit .....	2c
Merchandizing .....	7c
	<hr/>
Total Cost .....	34c

On this basis the housewife would still receive dried apples at a price comparable to what she would have to pay for fresh fruit.

There is a general impression that the cost of dehydration is an expensive process. The old sun drying method, or even the more modern dehydration methods, for prunes, peaches, apricots, apples, etc., have not proved expensive.

In vegetables the prices paid for individual products seem high due to the very high dry ratio. When considered on a fresh basis the cost is not so great, as is shown by the table above.

Many of these vegetables retail for much more than this in off seasons, and those products that are canned would cost much more as a canned product.

The actual costs of dehydration are not high. If we take potatoes, for example, the costs would run very low.

It is apparent that approximately half the cost is the cost of the raw product. Vegetables are being processed on a wartime basis and the cost of the vegetable itself is much higher than in peace-time.

On a comparative basis, however, canned products would run a much higher manufacturing cost in relation to the cost of the raw product.

During this war products will probably be manufactured both in Canada and the United States even if costs are much higher than normal. Whether or not dehydration will succeed after the war will depend on the maintenance of quality, education as to their use and economical manufacture of those lines suited to dehydration.

N.B.—The author acknowledges the grateful assistance of Cecil C. Eidt, Assistant in Charge of Fruit and Vegetable Processing, Department of Agriculture, Ottawa, for much of the authentic facts and research contained in this article on the Costs of Dehydrated commodities.

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